1999 Country Reports on Economic Policy and Trade Practices
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SAUDI ARABIA

Key Economic Indicators

(Billions of U.S. Dollars unless otherwise indicated)

	1997	1998	1999 1/ 2/
Income, Production and Employment:			
Nominal GDP	146.3	128.9	140.0
Real GDP Growth (pct)	1.9	1.6	1.0
GDP by Sector:			
Agriculture	8.9	9.1	N/A
Manufacturing (including oil)	13.5	12.6	N/A
Services	56.2	57.5	N/A
Government	36.7	34.2	N/A
Per Capita GDP (US$)	6,836	6,190	6,543
Labor Force (millions)	6.7	6.5	N/A
Unemployment Rate (pct)	N/A	N/A	N/A
Money and Prices (annual percentage growth):			
Money Supply Growth (M2)	6.6	2.4	N/A
Consumer Price Inflation	-0.4	-0.2	1.0
Exchange Rate (SR/US$ annual average)			
Official	3.745	3.745	3.745
Balance of Payments and Trade:			
Total Exports FOB	60.7	39.7	37.5
Exports to U.S.	9.4	5.1	N/A
Total Imports FOB	-26.4	-27.5	-27.4
Imports from U.S.	5.9	5.9	N/A
Trade Balance	34.2	12.1	10.0
Balance with U.S.	N/A	N/A	N/A
Current Account Deficit/GDP (pct)	0.3	-13	-5
External Public Debt	N/A	N/A	N/A
Debt Service Payments/GDP (pct)	4.7	5.3	5.1

Fiscal Deficit/GDP (pct)	1.1	8.8	N/A
Gold and Foreign Exchange Reserves	17.8	17.8	N/A
Aid from U.S.	0	0	0
Aid from All Other Sources	0	0	0

1/ 1999 figures are projections.

2/ Sources: IMF International Statistics Yearbook 1999; Saudi-American Bank Economic and Market Update; U.S. Embassy Riyadh 1999 Saudi Economic Trends Report; IMF Saudi Arabia Statistical Index.

1. General Policy Framework

Saudi Arabia generally sets a framework for a free market economy, but with parastatals dominating economic output. Government policies generally encourage commercial enterprise, but a strict interpretation of Islamic mores limits the range of policy options as well as that of commercial endeavors. Since about 1970, Saudi Arabia has published a series of five-year development plans, focusing on infrastructure and industrialization. Development plans, however, are presented as planning tools, not as centralized controls, and the government emphasizes that its development plans rely on significant private sector involvement.

The oil and government sectors are the engines of the economy. Parastatal enterprises, including Saudi ARAMCO (oil), Saudi Basic Industries Corporation (SABIC), and utilities, among others, tend to dominate the economy. Spending decisions taken by the few large state companies reverberate throughout the economy. Concerned with the security challenges posed by its neighbors, Saudi Arabia seeks sufficient military and security resources to protect its territory. The Saudis also protect the pilgrims who visit the two Islamic holy cities of Mecca and Medina. The kingdom is also a large buyer of advanced military technology.

In 1998, oil sector revenues comprised an estimated 37 percent of GDP, and an estimated 70 percent of budget revenues. Other government revenues, including items such as customs duties, investment income, and fees for services, are to a large degree indirectly tied to oil, as capital available for consumption and investment is generally derived from oil receipts. In addition, the manufacturing and services sectors are largely dependent on petroleum and petrochemical activities.

Starting with the oil boom dating from 1973, Saudi Arabia maintained annual budget surpluses until 1982, when the decline in oil prices led to a renewed deficit. These deficits have continued for the past 17 years. Initially, the deficits were financed by a drawdown of foreign exchange reserves. Starting in 1987, the government began financing deficits by issuing government bonds, and taking loans from domestic banks. The government has also accrued substantial arrearages to the private sector over the past decade, though these were paid down substantially in 1996 and 1997 with unanticipated oil revenues from these years.

Spending in 1996 exceeded the budgeted target by $12 billion, but because of high oil revenues, the government achieved its deficit target of $4.5 billion. Oil revenues were higher than anticipated for 1997 as well, allowing the government to end the year with a small $1.6 billion deficit. However, the collapse in oil prices in late November 1997 brought this favorable fiscal trend to an end. Saudi oil revenues dropped by 35 percent in 1998, leading to a deficit of $12.3 billion, or almost 10 percent of GDP. Oil prices have rebounded in 1999 and, coupled with increased fiscal discipline, have lowered the projected deficit to the $4-6 billion range. The government's hopes of achieving a balanced budget by 2000 depend mostly on what oil prices will be in that year.

Money supply is regulated through the Saudi Arabian Monetary Agency (SAMA), which has statutory authority to set monetary reserve requirements for Saudi Arabian banks, impose limits on their total loan portfolio, and regulate the minimum ratio of domestic assets to their total assets. It also manages the bond market, and can repurchase development bonds and treasury bills as required. There is a limit to the amount of bonds that can be repurchased. SAMA oversees a financial sector consisting of 10 commercial banks. All 10 banks have majority private ownership, with the exception of National Commercial Bank, where state institutions purchased 50 percent of total shares in 1999. The Ministry of Finance oversees five specialized credit institutions.

2. Exchange Rate Policy

The exchange rate for the Saudi Arabian Riyal is SR 3.745 = US$1.00. This rate has been consistent since 1986. Officially, the Riyal is pegged to the IMF's Special Drawing Rights (SDR) at SR 4.28255 = SDR 1. There are no taxes on the purchase or sale of foreign exchange.

Generally speaking, there are few foreign exchange controls for either residents or nonresidents, in keeping with the government policy to encourage an open economy. Of the few restrictions, the most noteworthy are: direct commercial transactions with Israel and Israeli-registered corporations are prohibited, as are most transactions with Iraq; and, local banks are prohibited from inviting foreign banks to participate in riyal-denominated transactions without prior SAMA approval.

3. Structural Policies

The government maintains price controls for basic utilities, energy, and many agricultural products. Water and electricity, for most consumers, are subsidized, with consumer prices often well below the cost of production, especially for potable water. Petroleum products and feedstocks for petrochemical industries are provided at below world market pricing, presumably reflecting discounts for lower costs in production and transport. The government maintains that local petroleum prices that are below world market averages (e.g., a gallon of gasoline sells for $.90 at the pump) reflect the low costs of production. Nonetheless, the effect of these low prices is that petroleum products, including many petrochemicals, are sold in Saudi Arabia at prices that effectively eliminate competing imports. Agricultural subsidies were dramatically curtailed in the early 1990s and have been reduced in recent budgets, in line with the government's deficit reduction plans and its goal to reduce water consumption.

The Saudi Arabian Government imposes few taxes, relying on oil revenues, customs duties, and licensing fees for most government revenue. Saudi Arabian nationals pay no income tax, but are obliged to pay "zakat," a 2.5 percent Islamic assessment based on net wealth (not income). Zakat is designed to support the Islamic community (e.g., to pay for hospitals, schools, support for the indigent). Saudi-owned businesses do not pay corporate tax beyond the "zakat." Foreign companies and self-employed foreigners pay an income tax, but do not pay zakat. Business income tax rates range from 25 percent on annual profits of less than $26,667 to a maximum rate of 45 percent for profits of more than $266,667. Some foreign investors avoid taxation either in part or totally, by taking advantage of various investment incentives, such as 10-year tax holidays for investments in approved projects meeting specified requirements. Import tariffs are generally 12 percent ad valorem (CIF), except on products imported from other member states of the Gulf Cooperation Council. Certain specified essential commodities (e.g., defense purchases) are not subject to custom duties. Saudi Arabia also levies a maximum 20 percent tariff on products that compete with local "infant" industries.

The Saudi Arabian Government is currently considering changes to the Foreign Investment Code and related foreign corporate taxation laws, which may result in significant reductions in the amount foreign corporations are taxed. Changes to Saudi Arabia’s tariff structure are also being considered in the context of Saudi Arabia’s effort to gain membership in the World Trade Organization.

4. Debt Management Policies

Saudi Arabia is a net creditor in world financial markets. SAMA manages foreign assets of roughly $54 billion in its issues and banking departments, and an estimated $29 billion for autonomous government institutions, including the Saudi Pension Fund, the Saudi Fund for Development, and the General Organization for Social Insurance. Under SAMA's rules, $17.8 billion of the roughly $54 billion in foreign assets is designated to guarantee the Saudi Riyal. In addition to overseas assets managed by SAMA, the commercial banking system has an estimated net foreign asset position of $11.4 billion.

Public sector foreign debt, which stood at a level of $1.8 billion at the beginning of 1995, was retired in May of that year. Domestic banks, Saudi ARAMCO, Saudi Arabian Airlines, and other state-owned enterprises, however, have overseas liabilities.

Government domestic borrowing has a short history in Saudi Arabia. The government began borrowing to finance budget deficits in 1987 by selling government development bonds having two-to-five year maturities. After the massive defense expenditures of the 1991 Gulf War, the government expanded its borrowing by signing loan syndications with international and domestic banks, and by introducing treasury bills. This debt, owed almost entirely to domestic creditors, such as autonomous government institutions, commercial banks, and individuals, ballooned to about $130 billion by the end of 1998, or over the GDP level. In addition, the government issued a series of bonds to farmers and some other private sector creditors (mainly contractors) for past due amounts. Paying down this debt is now a focus of government concern.

Non-governmental external debt stood at $28 billion in 1998, up from $16 billion in 1996. This debt is serviceable, especially in light of improved oil revenues.

5. Significant Barriers to U.S. Exports

Saudi Arabia is currently in the process of negotiating accession to the World Trade Organization (WTO). This may result in changes to a number of current regulations that have the potential to restrict entry of U.S. exports and investments.

Import licensing requirements protect Saudi Arabian industries or enhance Saudi Arabian businesses. In most cases, foreign companies must operate through a Saudi Arabian agent. Contractors for public projects must purchase equipment and most supplies through Saudi agents. (This agency requirement does not apply to defense-related imports.) Saudi Arabia requires licenses to import agricultural products.

Saudi Arabia's preshipment inspection regime, known as the International Conformity Certification Program (ICCP), is designed to protect Saudi Arabian consumers from inferior foreign products. The ICCP has elements that can be viewed as barriers to free trade -- such as an ad valorem-based fee schedule -- and remains controversial. It adds inspection costs to imported civilian products, may delay shipments to Saudi Arabia, and can increase exporter overhead.

Restrictions on shelf life labeling standards in Saudi Arabia may make it difficult for some U.S. food producers to compete in the Saudi market.

Saudi Arabia gives preference to imports from other members of the Gulf Cooperation Council (GCC) in government purchasing, with a 10 percent price preference over non-GCC products for government procurement.

Saudi Arabia requires foreign civilian contractors to subcontract 30 percent of the value of government non-military contracts, including support services, to firms having Saudi-majority ownership. Many firms have reported that this has not been enforced consistently. Some U.S. businessmen have complained that this is a barrier to the export of U.S. engineering and construction services. Other service industries are restricted to government-owned companies, e.g., certain insurance and transportation services.

The "Investment of Foreign Capital Regulation" establishes the following conditions for a non-Saudi national to obtain a license for a business and for investment of foreign capital (considerable revisions to the Regulation are nearing completion):

a. Foreign capital must be invested in a development project, or in projects within the framework of the development plan in effect at the time of the investment. Investments in oil and mineral sectors are subject to special regulations of the Ministry of Petroleum and Mineral Resources.

b. Foreign capital investment must be accompanied by foreign technical expertise. In addition, the "foreign capital investment committee," established by the "investment of foreign capital regulation," reviews license applications. The committee's screening of foreign investments is general; the criteria for screening, other than the two conditions listed above, appear to be limited to:

-- Ensuring that an investment does not violate the social or religious mores of Saudi Arabia.

-- Regulating the number of establishments in any one sector, to the level that the market will sustain.

There is no requirement that a non-Saudi investor have a Saudi partner. At the same time, businesses having a minimum of 25 percent Saudi ownership are eligible for soft government loans, which are generally unavailable to firms lacking Saudi ownership. The government is currently reviewing foreign investment and agency regulations.

Saudi labor law requires companies to employ Saudi nationals, but foreigners account for at least 90 percent of the private sector labor force. Large companies are required to increase their percentage of Saudi employees by a certain percentage annually or face restrictions. This emphasis on "Saudiization" is increasing as the number of unemployed/underemployed Saudis increases.

6. Export Subsidies Policies

Saudi Arabian planners say that there are no export subsidy programs for industrial projects. Because feedstock prices are relatively low in Saudi Arabia, industrial production of petroleum and related downstream products is comparatively attractive. The government argues that this is simply a reflection of the low cost of domestic oil production. On January 1, 1998, the Saudi Government announced a 50 percent across-the-board increase in natural gas prices from $.50/million btu to $.75/million btu. The government has reduced subsidies to agriculture, which has resulted in reduced agricultural production available for export.

7. Protection of U.S. Intellectual Property

Saudi Arabia has applied to join the World Trade Organization (WTO). As part of its accession effort, Saudi Arabia is revising all of its intellectual property laws to make them conform with the WTO's Trade Related Aspects of Intellectual Property (TRIPs) standards. Saudi Arabia remains on the USTR's "Special 301 Watch List," having moved up in 1996 from the program's "Priority Watch List" in recognition of progress made in intellectual property rights protection. Saudi Arabia has joined the Universal Copyright Convention, and is a member of the World Intellectual Property Organization (WIPO), though not a contracting party to any of the treaties administered by WIPO. Efforts to protect intellectual property rights are uneven, and audio, video and software companies want greater protection of their product content in the Kingdom.

Saudi Arabia has enacted a patent regulation and established a patent office. The regulation was patterned along the lines of the U.S. patent law, but does not reproduce it. The terms of patent protection are generally adequate, but the period of protection is 15 years, five years less than the international TRIPs standard. The regulation permits compulsory licensing if the patent holder refuses to use the patent, or for other public policy reasons, on a wider basis than permitted under TRIPs. Further, the Saudi Patent Office is functionally slow. The office has received several thousand patent applications since 1989, but has completed action on only a relative handful. The patent office lacks sufficient manpower to process the backlog of applications. The Gulf Cooperation Council (GCC) established a parallel patent office in October 1998, but that office is not yet issuing patents.

Registration of trademarks is relatively uncomplicated, although some companies have complained that registration and search fees are high. Although legal remedies for infringement of a trademark exist, enforcement of trademark protection is inconsistent.

The embassy has received no verifiable reports of book piracy, and only one report of the unlicensed use of a published photograph. Piracy of U.S.-produced audio and videocassettes has decreased due to government enforcement polices but remains a problem. Estimates of losses to computer software companies due to illegal copying vary widely, but are generally considered high.

8. Worker Rights

a. The Right of Association: Saudi regulations prohibit labor associations.

b. The Right to Organize and Bargain Collectively: Expatriates perform much skilled and almost all unskilled labor. Non-Saudi workers who seek to organize may be deported.

c. Prohibition of Forced or Compulsory Labor: Forced labor is prohibited. However, as most unskilled labor is performed by expatriates, and as Saudi employers have legal authority over the movement of their contracted laborers, low paying labor may occur, especially in the case of domestic servants and in remote areas. During the past three years, the government has expelled many workers without proper work permits. One result of this may be to reduce the potential for abuse.

d. Minimum Age for Employment of Children: The labor law states that "a juvenile who has not completed 13 years of age shall not be employed." This restriction may be waived by application to the Ministry of Labor with the consent of the juvenile's parent or guardian. Children under 18 and women may not be employed in hazardous or unhealthy occupations. Wholly-owned family businesses and family-run farms are exempt from these rules.

e. Acceptable Conditions of Work: Saudi Arabian authorities consider that provisions of Islamic Law (the Shariah) provide more than adequate protection for laborers, and therefore additional regulation is unnecessary. Conditions of labor, while far from perfect, may in some cases be better than those found in countries from which most poorer expatriates come. Although Saudi Arabia has no minimum wage, generally speaking, expatriate laborers come to Saudi Arabia because they can earn more than they could at home. They receive time-and-one-half for hours (up to 12) over the 44 hours normally worked per week. The labor law requires employers to provide health insurance and to protect workers from job-related hazards and diseases.

f. Rights in Sectors with U.S. Investment: Worker rights in sectors with U.S. investment do not differ from those elsewhere. Conditions of work at major U.S. firms and joint-venture enterprises are generally better than elsewhere in the Saudi economy. Workers in U.S. firms normally work a five to five-and-one-half day week (i.e., 44 hours) with paid overtime. Overall compensation tends to be at levels that make employment with U.S. firms attractive.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment in Saudi Arabia on a Historical Cost Basis – 1998. Generally it is assumed that the true value of U.S. direct investment in Saudi Arabia is in the range of $7-8 billion with the large majority in the petrochemical field. Antitrust concerns and general difficulties in gathering statistics make the exact aggregation of data impossible.

(Millions of U.S. Dollars)

Category		Amount
Petroleum		270
Total Manufacturing		149
Food & Kindred Products	14	
Chemicals & Allied Products	(1)	
Primary & Fabricated Metals	20	
Industrial Machinery and Equipment	(1)	
Electric & Electronic Equipment	1	
Transportation Equipment	5	
Other Manufacturing	51	
Wholesale Trade		105
Banking		(1)
Finance/Insurance/Real Estate		1,533
Services		280
Other Industries		(1)
TOTAL ALL INDUSTRIES		4,209

(1) Suppressed to avoid disclosing data of individual companies.

Source: U.S. Department of Commerce, Bureau of Economic Analysis.